

Message Text

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E.O. 11652: GDS

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SUBJECT: U.S. AND INDONESIAN ENERGY ISSUES: DISCUSSION OF
PACIFIC-INDONESIAN LNG CONTRACT WITH MINISTERS WIDJOJO AND
PRAWIRO AND GENERAL HARYONO ON AUGUST 7

REF: A. STATE 194528, B. JAKARTA 10615

1. FOLLOWING IS THE FULL TEXT OF THE MEMCON PREPARED BY
THE DEPARTMENT OF ENERGY ON THE DISCUSSIONS BETWEEN ENERGY
SECRETARY SCHLESINGER AND HIGH INDONESIAN OFFICIALS ON
AUGUST 7.

2. QUOTE: MINISTER WIDJOJO OPENED BY MENTIONING THE
ENCOURAGING DEVELOPMENTS IN THE PACIFIC LIGHTING LNG PRO-
JECT, AND ASKED FOR SECRETARY SCHLESINGER'S ASSESSMENTS.

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THE SECRETARY RESPONDED BY SAYING THAT THIS WAS A LIVELY
ISSUE, THAT HE WAS INHIBITED FROM DISCUSSING THIS BECAUSE
IT WAS A PENDING REGULATORY MATTER, BUT THAT THE CONCEPT OF
THE PROJECT HAD BEEN APPROVED. HE EMPHASIZED HIS RELUC-
TANCE TO HAVE GAS PRICES WHETHER PIPELINE OR LNG, TIED TO
OPEC PRICES. HE ADDED THAT THE U.S. INDEX PROBLEM APPEARED
TO HAVE BEEN SOLVED WITH THE ADOPTION OF A MORE GENERAL
U.S.-BASED INDEX. HE DIFFERENTIATED THIS KIND OF INDEX
FROM OPEC-PRICED INDICES WHICH WERE DETERMINED BY "ADMIN-

ISTRATIVE EXUBERANCE." CONCERNING THE OTHER HALF OF THE PRICE ESCALATOR, THE SECRETARY SAID THAT WE WOULD LOOK AT THIS VERY CAREFULLY.

LOOKING INTO THE FUTURE, THE SECRETARY ANTICIPATED AN EXCESS OF GAS SUPPLY OVER DEMAND, A SITUATION DIAMETRICALLY OPPOSED TO EXPECTED OIL MARKET DEVELOPMENTS. CONSEQUENTLY, TYING GAS PRICES TO FUTURE OIL PRICES WOULD TRANSFER THE ANTICIPATED OIL MARKET STRINGENCY TO GAS PRICING, AND THE SECRETARY EMPHASIZED THAT HE WOULD BE RELUCTANT TO SEE SUCH A TIE. CONCERNING THE GENERAL ISSUE OF SITING, THE SECRETARY EXPRESSED THE BELIEF THAT PROGRESS WAS UNDERWAY.

MINISTER WIDJOJO RESPONDED, SAYING THAT HE WAS HAPPY TO NOTE THE GENERAL CONSENSUS IN CALIFORNIA. THE SECRETARY POINTED OUT THAT AT THE STATE LEVEL THERE CONTINUED TO BE THE POSSIBILITY OF ENVIRONMENTAL OPPOSITION, AND REFERRED TO THE PROBLEMS OF APPROVING THE SOHIO PIPELINE. HE EMPHASIZED THAT IN PRINCIPLE AT THE FEDERAL LEVEL THE SALE OF LNG HAS BEEN ACCEPTED.

ON THE ISSUE OF PRICE, MINISTER WIDJOJO STATED THAT INDONESIA HAD GONE A LONG WAY TO ADJUST ITS POSITION AND HOPED
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THAT THE REVISIONS IN THE ESCALATOR WILL MEET WITH U.S. APPROVAL. HE EXPRESSED HIS CONCERN ABOUT THE IMPACT OF U.S. CLAUSES ON JAPAN, AND HOPED THAT THE U.S. ARRANGEMENTS WOULD NOT HAVE AN ADVERSE EFFECT ON JAPAN. SECRETARY SCHLESINGER STRESSED THE GREAT DIFFERENCES IN MARKET CONDITIONS BETWEEN THE UNITED STATES AND JAPAN, PARTICULARLY TRANSPORTATION. MINISTER WIDJOJO STRESSED THAT IT WAS IMPORTANT FOR HIS GOVERNMENT TO AVOID A "DOWNWARD SPIRAL" EFFECT BETWEEN DIFFERENT U.S. AND JAPANESE TERMS WITH RESPECT TO INDONESIAN GAS. SECRETARY SCHLESINGER EMPHASIZED THAT THE MARKET SHOULD REFLECT FACTORS SUCH AS TRANSPORTATION DISTANCE, AND THAT IN THIS REGARD JAPAN IS A MORE NATURAL MARKET FOR INDONESIAN GAS. HE ADDED THAT SINCE THE UNITED STATES HAS ALTERNATIVE HYDROCARBON SOURCES, JAPANESE DEMAND IS "BETTER DEFINED." HE STRESSED THAT FOR THE UNITED STATES LNG IS A "MARGINAL RESOURCE"; IN SEQUENCE, THE PREFERRED NATURAL GAS SOURCES ARE DOMESTIC LOWER 48 GAS. ALASKAN GAS, SYNTHETIC GAS FROM COAL, AND GAS FROM CANADA AND MEXICO; TURNING THEN TO LNG, PRICE BECOMES A CRUCIAL QUESTION.

MINISTER WIDJOJO AGREED THAT JAPAN IS INDEED A NATURAL MARKET FOR INDONESIA. HE ADDED THAT IF THE U.S. DECISION CONCERNING THE PACIFIC LIGHTING PROJECT IS NEGATIVE, HE WOULD NOT WANT INDONESIA'S POTENTIAL ACCESS TO JAPAN TO BE

PREEMPTED; CONSEQUENTLY, HIS GOVERNMENT HOPES FOR AN EARLY

DECISION.

SECRETARY SCHLESINGER STATED THAT IN PRINCIPLE A GO-AHEAD DECISION HAD BEEN RENDERED ON THE PACIFIC LIGHTING PROJECT, SUBJECT TO AGREEMENT ON ESCALATORS, AND SUBJECT TO RESOLUTION OF THE CALIFORNIA SITING ISSUE. HE ADDED THAT AT THE STATE LEVEL, HE ASSUMED THAT SOME FORM OF INCREMENTAL PRICING WOULD BE ADOPTED.

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GENERAL HARYONO INTERVENED, ADDING THAT INDONESIA HAD BEEN WAITING ON THIS PROJECT FOR A CONSIDERABLE TIME, THAT THE NATURAL MARKET IS INDEED JAPAN, THAT THE INITIAL CONTRACTS HAD TAKEN CARE OF FACTORS SUCH AS DISTANCE, AND THAT WITH CHANGES IN THE ESCALATION PROVISIONS, THE DIFFERENCES BETWEEN THE U.S. AND JAPANESE CONTRACTS ARE WIDENING. HE MENTIONED THAT HIS GOVERNMENT HAD AUTHORIZED PACIFIC LIGHTING TO MAKE CHANGES NECESSARY TO MEET DOE WISHES, AND TO REFILE THE APPLICATION.

SECRETARY SCHLESINGER ASKED ABOUT THE SIZE OF THE JAPANESE GAS MARKET. GENERAL HARYONO EXPLAINED THAT THERE ARE TWO PRINCIPAL GROUPS OF BUYERS, AND THAT WHILE HE WISHED TO RETAIN A BALANCE BETWEEN THE JAPANESE AND THE WEST COAST MARKETS, CONCEIVABLY UP TO 10 TRAINS COULD BE DEDICATED TO THE JAPANESE MARKET. SECRETARY SCHLESINGER RE-EMPHASIZED THAT PRICES SHOULD BE DETERMINED BY GAS MARKET FORCES RATHER THAN OIL MARKET FORCES. GENERAL HARYONO RESPONDED, SAYING THAT HE BELIEVED THAT MORE LNG COULD BE SOLD TO JAPAN, AND THAT GAS COULD ALSO BE USED DOMESTICALLY TO FREE UP OIL EXPORTS. HE ADDED THAT WITH THE PASSAGE OF TIME THE JAPANESE INTEREST WAS BECOMING MORE ACTIVE, AND THAT THE JAPANESE WERE ALSO KEENLY INTERESTED IN THE TANKER QUESTION, PARTICULARLY ON THE INDONESIA-JAPAN ROUTE.

MINISTER RADIUS, AT THE INVITATION OF MINISTER WIDJOJO, DISCUSSED THE ORIGINS OF THE U.S. AND JAPANESE VENTURES, EMPHASIZING THE RAPIDITY WITH WHICH THE JAPANESE VENTURE HAD PROGRESSED, THE CHANGES IN THE POLITICAL SITUATION BETWEEN 1974 AND 1977, THE NEED TO PUT LNG IN THE FRAMEWORK OF COOPERATION, AND THE NEED FOR INDONESIA TO GET THE BEST PRICES FOR ITS PRODUCTS -- NOTING THAT OIL ACCOUNTS FOR 70 PERCENT OF HIS GOVERNMENT'S REVENUE. HE CONCLUDED

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BY ASKING SECRETARY SCHLESINGER FOR HIS ADVICE ON WHETHER
"WE SHOULD MOVE."

SECRETARY SCHLESINGER EMPHASIZED THAT THE LNG MARKET IN
THE UNITED STATES WOULD REMAIN LIMITED UNLESS DOMESTIC GAS
PRODUCTION PROVED DISAPPOINTING. STRESSING THAT LNG IS
"NOT OUR PREFERRED ROUTE," HE ADDED THAT WE WOULD BE

PREPARED TO BUY LNG, IF IT WERE ADVANTAGEOUS COMPARED WITH
IMPORTED CRUDE. HE STRESSED THAT HE WOULD NOT MAKE LNG
PLANS BASED ON THE EXPECTATION OF AN ENORMOUSLY EXPANDING
MARKET IN THE UNITED STATES. HE CONCLUDED BY SAYING THAT
LARGE-VOLUME LNG PROJECTS WOULD BE INHIBITED IN THEIR
ACCESS TO THE U.S. MARKET BY TRANSPORTATION DISTANCES AND
BY DOMESTIC U.S. PRODUCTION.

GENERAL HARYONO SHIFTED THE DISCUSSION TO THE POSSIBILITY
OF ALASKAN CRUDE EXPORTS TO JAPAN. SECRETARY SCHLESINGER
EMPHASIZED THE REGULATORY CONSTRAINT ON SUCH A STEP, AND
ADDED THAT IF THE REGULATORY CONSTRAINT WERE EASED, THIS
WOULD REDUCE PRESSURES TO CREATE AN INLAND TRANSPORTATION
SYSTEM. HE MENTIONED THAT THE JAPANESE ARE EXCEEDINGLY
INTERESTED IN ALASKAN CRUDE FOR POLITICAL AND BILATERAL
TRADE REASONS. HE EMPHASIZED THAT THE PIPELINE CAPACITY
WOULD BUILD UP TO 1.5 - 1.6 MILLION B/D BY THE EARLY
1980'S, AND WOULD REQUIRE A DECADE TO GET UP TO 2 MILLION
B/D. HE EMPHASIZED THAT IF THERE WERE TO BE ANY EXPORT
OF CRUDE TO JAPAN, THESE EXPORTS WOULD BE LIMITED TO
ADDITIONS TO ALASKAN CAPACITY ABOVE THE EXISTING LEVEL OF
1.2 MILLION B/D. IN SUMMING UP, MINISTER WIDJOJO STATED
THAT HE HOPED THE UNITED STATES WOULD REACH A FAVORABLE
DECISION ON THE PACIFIC LIGHTING PROJECT AS SOON AS
POSSIBLE, EMPHASIZING THAT THE VOLUME MIGHT BE SMALL FOR
THE UNITED STATES BUT REPRESENTED A LARGE EXPORT EARNER
FOR INDONESIA.

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SECRETARY SCHLESINGER ASKED FOR THE INDONESIAN VIEW OF OIL
MARKET DEVELOPMENTS. GENERAL HARYONO RESPONDED, SAYING
THAT THE CURRENT DIFFICULTIES APPEAR TEMPORARY AND THAT
MARKET BALANCE SHOULD BE RESTORED BY THE END OF 1979.
HOWEVER, IF THE MARKET WERE TO REMAIN FLAT, INDONESIA
MIGHT HAVE TO CUT BACK PRODUCTION BY 150,000 B/D, FOREGOING
DOLS 400 MILLION. GENERAL HARYONO ADDED THAT 1977 HAD
BEEN A VERY GOOD YEAR FOR THEM, BUT THAT HE RECOGNIZED
ITS NONRECURRING NATURE.

SECRETARY SCHLESINGER DESCRIBED EXPECTED OIL MARKET
DEVELOPMENTS, STRESSING THAT ALTHOUGH SUPPLY IS CURRENTLY
PLENTIFUL, WITH DEMAND INCREASING AT 2 MILLION B/D A YEAR,

SURPLUS SUPPLY WOULD CERTAINLY BE DRAINED BY 1985. HE SURMISED THAT THE RECENT REDUCTION IN INDONESIAN PRODUCTION WAS A PRICE RESPONSE BY BUYERS. HE ADDED THAT THE ALASKAN PIPELINE WAS PUT IN THE WRONG PLACE, AND SHOULD HAVE GONE TO THE MID-WEST; AS A RESULT OF THE PIPELINE, THERE IS NOW A PACIFIC OIL GLUT. HE MENTIONED THAT IF JAPANESE OIL SWAPS WERE APPROVED, THE PRESSURE ON U.S. REFINERS TO ADJUST TO ALASKAN CRUDE WOULD BE ALLEVIATED.

GENERAL HARYONO EXPRESSED HIS CONFIDENCE THAT INDONESIAN LIGHT CRUDE WOULD STILL HAVE A MARKET ON THE WEST COAST. SECRETARY SCHLESINGER POINTED OUT THAT INDONESIA HAD A NATURAL ALLY IN SOME OF THE STATE REGULATORY BOARDS."
END QUOTE

3. OFFICIALS IN ATTENDANCE AT THE MEETING WERE:

FOR INDONESIA

DR. WIDJOJO NITISASTRO, COORDINATING MINISTER FOR
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ECONOMICS, FINANCE AND INDUSTRY
AMBASSADOR D. ASHARI, INDONESIAN AMBASSADOR TO THE U.S.
DR. RADIUS PRAWIRO, MINISTER FOR TRADE AND COOPERATIVES
MAJOR GENERAL PIET HARYONO, PRESIDENT-DIRECTOR OF PERTAMINA

FOR THE UNITED STATES

JAMES R. SCHLESINGER, SECRETARY, DEPARTMENT OF ENERGY
HARRY E. BERGOLD, JR., ASSISTANT SECRETARY, DOE/IA
RICHARD C. HOLBROOKE, ASSISTANT SECRETARY, EA
PETER BORRE, DOE/IA/DAS:TR
SARAH R. JACKSON, DOE/IA/DAS:PD
ROBERT GOODWIN, DOE/OGC

CHRISTOPHER

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